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IN THE

Supreme Court of the United States

OCTOBER TERM, 1956

No. 60

ROBERT W. JAFFKE, *Petitioner*

v.

WILLIAM C. DUNHAM, Trustee of the Estate of ROBERT L. KNETZER, Bankrupt, *Respondent*

On Writ of Certiorari to the United States Court of Appeals For the Seventh Circuit

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BRIEF FOR PETITIONER

OPINION BELOW

The opinion of the United States Court of Appeals for the Seventh Circuit is reported in 229 F. 2d 232. The decision of the district court is not officially reported but is set forth at R. 164-167.

JURISDICTION

The judgment of the Court of Appeals was entered on January 13, 1956. The judgment was modified by the Court of Appeals on February 13, 1956. The petition for a writ of certiorari was filed on April 11, 1956, and was granted on May 28, 1956 (R. 202). This Court has jurisdiction under 11 U.S.C. § 47 and 28 U.S.C. § 1254.

QUESTIONS PRESENTED

Where the losing party in the district court (Respondent) appeals to the Court of Appeals, and the prevailing party (Petitioner) took no cross appeal from adverse evidentiary rulings by the district court, did the appellate court err in reversing the judgment and ordering judgment for appellant, holding certain findings unsupported by evidence, refusing to consider in the absence of a cross appeal evidence supporting such findings adduced by Petitioner but stricken by the trial court?

Where a federal district court, sitting as a bankruptcy court, adjudges a bankrupt in contempt and sentences him to jail for non-compliance with a turnover order, but the bankrupt is released from imprisonment on numerous occasions over a two year period to locate money to comply with the turnover order, and the bankrupt fraudulently obtains money from an innocent third party and pays it to the Trustee in Bankruptcy to purchase his freedom, does the Trustee in Bankruptcy as an officer of the court have the duty to investigate the source of such payments?

STATEMENT

On October 21, 1948, Robert L. Knetzer was adjudged bankrupt by the United States District Court for the Southern District of Illinois (R. 165). On December 3, 1948, William C. Dunham, Respondent here, was appointed Trustee in Bankruptcy of the Knetzer Motor Sales Company. On December 10, 1948, he was appointed Trustee in Bankruptcy of the Robert L. Knetzer Estate (R. 76).

The Bankrupt's Estate was hopelessly insolvent (R. 182). Knetzer Motor Sales Company was in an equally hopeless position (Def. Exh. 1, R. 161-164, 138). Before his bankruptcy, the Bankrupt had persuaded many persons to make large deposits on automobiles and tractors which were never delivered (R. 182).*

The Turnover Order

On July 11, 1949, approximately nine months after the bankruptcy, the District Court found that the Bankrupt, Knetzer, had concealed assets of his Estate and entered a turnover order requiring him to pay Respondent "forthwith" $250,000. The order specifically recited that hearing had been held in both the Estates of Robert L. Knetzer and Knetzer Motor Sales Company, Bankrupts; that Respondent as Trustee for Knetzer Motor Sales Company was *not* entitled to any turnover order against Knetzer; and that monies recovered were to be held by Respondent as Trustee for the Estate of Robert L. Knetzer (Pet. Exh. 1, R. 137, 144).

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* R. W. Jaffke, Petitioner, was one of those who made such a deposit. Upon Knetzer's bankruptcy he filed a claim as a general creditor (R. 44, 47). This claim is not involved in this case.

On December 1, 1949, the Bankrupt, upon Respondent's petition to show cause, was found guilty of contempt of court for failure to comply with the turnover order (Pet. Exhs. 2, 3, 4, R. 137, 145-148). The sentence to jail for contempt was stayed, however, until February 18, 1950 (Pet. Exh. 4, R. 137, 149). On March 28, 1950, the Bankrupt was sent to jail.

He was permitted to leave jail on different occasions in the custody of a United States Marshall upon promising that he would use his freedom to obtain sufficient assets to comply with the turnover order (R. 181). On "many occasions" when the Bankrupt was out of jail he approached Respondent and promised to make payments on the turnover order at some definite time in the future. Respondent would then call his attorney or the district judge to obtain permission for the Bankrupt to remain out of jail (R. 85). Respondent, of course, knew that the Bankrupt had been jailed and had "been in and was out and back in again." (R. 85). The Bankrupt while on these excursions from jail made installment payments to Respondent on the turnover order, in effect buying further freedom from imprisonment (R. 77-82). This continued until February, 1952.

Payments on the turnover order were also made by third persons.

Fraud on Petitioner

On December 6, 1950, over a year after the Bankrupt had been adjudged in contempt, Petitioner was contacted by the Bankrupt (R. 49-51). He told Petitioner of the Bison Mining and Development Company which was to build a large scale housing development (R. 49-50). Knetzer convinced Petitioner that

there were large profits to be made, and based upon representations found by the trial and appellate courts to be fraudulent, Petitioner gave him $2300 (R. 50-51, 53). Later the same day Petitioner gave him an additional $3800 upon the representation by the Bankrupt that he needed the additional money to pay into Court on his Bankruptcy account. The Bankrupt stated that he had agreed to make the payment to the court under duress (R. 53-54). He told Petitioner that $3,800 payment to the court would give him sufficient time to complete the Bison Company "deal." (R. 54) At the time of the two meetings the Bankrupt was not in the custody of any third person or a United States Marshall (R. 51).

Petitioner saw or heard from Knetzer from time to time during the ensuing period and at no time was he ever in custody (R. 57). Petitioner made further payments to the Bankrupt totalling $47,980.00. These payments were further investments in the Bison Company. The last payment was made on October 22, 1951* (R. 109). The trial court found, which finding was affirmed on appeal, that during the period December 7, 1950 to October 23, 1951, the Bankrupt defrauded Petitioner of the sum of $47,980.00 (R. 109).

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* To summarize, Petitioner made the following payments to the Bankrupt on the dates indicated:

12- 7-50	$ 6,100.00	1- 8-51	$ 1,000.00
12-13-50	12,500.00	3-14-51	520.00
12-18-50	7,500.00	6-21-51	260.00
12-22-50	9,000.00	9- 1-51	360.00
1- 3-51	6,000.00	10-21-51	2,000.00
		10-22-51	2,800.00
		Total	$47,980.00

The Bankrupt's Admission

Petitioner learned for the first time in the spring of 1952 that the Bankrupt had not used the money for the Bison Mining and Development Company. He discovered that the Bankrupt had instead paid Thirty-six Thousand Dollars ($36,000.00) of the $47,980.00 to Respondent (R. 110-112). Based on information from the Bankrupt, Petitioner prepared an affidavit for the Bankrupt's signature (Pet. Exh. 24, R. 203, 112). This affidavit was presented to the Bankrupt by the Bankrupt's attorney, R. W. Heinze, who warned the Bankrupt that he could not sign it if it were not true (R. 103-104). The Bankrupt signed the affidavit before a notary after being sworn (R. 105, 74-76). The affidavit contains an admission by the Bankrupt that he obtained $47,980.00 from Petitioner from December 7, 1950 to October 23, 1951, and that he paid $36,000.00 of that sum to Respondent as Trustee "for the purposes of remaining out of jail." (R. 203).

Petitioner's Suit

On December 1, 1952, Petitioner filed his petition to recover $47,980.00 from the Bankrupt and $36,000.00 from Respondent. On August 26, 1953, the Bankrupt Knetzer died (R. 35).

At the trial, Respondent, called as an adverse party by plaintiff, testified as follows. During the period from December 7, 1950 to November 1, 1951, he received installment payments on the turnover order totalling $75,923.72 from the Bankrupt and one Saul Cohn (Tr. 87). Respondent knew Cohn was an attorney but he did not know whom Cohn was representing nor did Respondent know where Cohn obtained the money (R. 79-80). Respondent never made any

inquiry of Knetzer as to where he obtained the money paid in under the turnover order (R. 87). Respondent never had any evidence that the payments made under the turnover order were from concealed assets of the Estate (R. 93-94).

Respondent knew that the Bankrupt was out of jail on many occasions *not* in the custody of a Marshall (R. 77). There is no evidence that Respondent inquired why the Bankrupt was not in custody when free of confinement. Respondent, at the Bankrupt's suggestion, would request the court to grant the Bankrupt additional time out of jail (R. 85).

Respondent requested this additional freedom even though he had heard testimony under oath that the Bankrupt had been obtaining money from third parties. This testimony was given at creditors' meetings as early as April 13, 1950 (R. 84, 90-91, 38-39). Additionally, third persons made payments to Respondent purportedly under the turnover order (R. 80, 82, 83, 84).

The Bankrupt gave the Respondent many different reasons why he could not pay the entire amount required by the turnover order (R. 87). He told the Respondent of many "business ventures" (R. 86), including the "Christmas tree" and "Teapot Dome deals" (R. 83, 86). Respondent, with knowledge of the above facts, failed to make any inquiry as to the source of money paid to him (R. 80, 78-79, 87). Respondent had no evidence that money paid in was from concealed assets (R. 93-94). Respondent remembered his testimony at a grand jury hearing in 1952 "very well" (R. 88). Yet Respondent *could not deny* that he may have testified at the hearing that he had received

in excess of $5,000.00 from the Bankrupt in 1951, which the Bankrupt told him had been obtained from Petitioner (R. 88-89).

Ralph Riley, another investor, testified that he had paid the Bankrupt $32,389.00 between June 28, 1950 and September 12, 1950 (R. 140). Petitioner in his brief to the trial court requested the court to take judicial notice that Respondent had received payments under the turnover order of $32,076.28 in the period June 28, 1950 to October 28, 1950 (R. 193). Petitioner testified that the Bankrupt obtained $47,980.00 from him during the subsequent period, December 7, 1950 through October, 1951.

Another witness, Clint Petty, testified he paid the Bankrupt $44,000.00 from April 14, 1951 through May, 1951 (R. 138-139). Respondent received $75,923.72 under this turnover order during the period December 7, 1950 through October, 1951 (R. 87). Subtracting the entire $44,000.00 Petty paid the Bankrupt from the total received by Respondent during the above period leaves a balance of $31,923.72.

It was stipulated at trial that one Sammons, if present, would testify that he paid the Bankrupt $101,550.00 during the period *November* 1, 1951 to February, 1952 (R. 138).*

The Decision of the Trial Court

The trial court, at the conclusion of the trial and after receiving briefs from the parties, found that the Bankrupt during the period December 6, 1950 to November 1, 1951, had obtained large sums of money

* The court of appeals erroneously stated the stipulation covered a period from *October* 1, 1951 (R. 185).

from Petitioner by fraud and misrepresentation. The court further found that $27,400 of the money so obtained from Petitioner was delivered over to Respondent as Trustee in Bankruptcy* who had possession of $27,400 that belonged to Petitioner. The court concluded that the equities of the case were with Petitioner. The court entered judgment for Petitioner for $27,400. The court, however, sustained Respondent's motion to strike Petitioner's Exhibit 24, the affidavit of the Bankrupt.** (R. 164-167). The findings and judgment of the trial court are found at R. 164-167.

The Decision of the Court of Appeals

Respondent appealed and the court of appeals reversed (R. 179-186). The court of appeals sustained the finding of the lower court that the Bankrupt had defrauded Petitioner of $47,980. The court ruled, however, that the evidence in the record was not sufficient to support a finding that the Bankrupt had paid $27,400 of this money to Respondent. The court refused to pass on whether the trial court had properly stricken the affidavit of the Bankrupt Knetzer, stating

> "There was no cross-appeal by the petitioner to question this action by the trial court, and this court may not consider Knetzer's affidavit as evidence in this case" (R. 183).

The court then declared that without the affidavit of Knetzer there was no sufficient evidentiary basis to

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* Significantly the judge stated at the conclusion of the trial: "I don't think the Court can be very much confused about the facts of the money paid in" (R. 143).

** The Honorable J. Leroy Adair who presided at the trial died January 19, 1956.

support the finding of the trial court that the Bankrupt had paid $27,400 of Petitioner's money to Respondent. The judgment of the trial court was reversed and the cause remanded for further proceedings.

On Respondent's motion to modify the mandate (R. 187), however, the appellate decision was modified to provide that the cause be remanded "with instructions to enter judgment for the respondent-appellant" (R. 186).

SUMMARY OF ARGUMENT

I

A. Where an appeal is taken by the losing party from a judgment of the district court, the victorious party may support the judgment on appeal on any ground raised below. *United States* v. *American Ry. Exp. Co.*, 265 U.S. 425 (1924); *Anderson* v. *Atherton*, 302 U.S. 643 (1937); *Langnes* v. *Green*, 282 U.S. 531 (1931). He may urge affirmance of the judgment on grounds not considered, or which were overlooked by the trial court. *Ibid.*, *Morley Construction Co.* v. *Maryland C. Co.*, 300 U.S. 185 (1937). Petitioner, seeking to support the findings and judgment favorable to him, had the right to urge that evidence improperly stricken at the trial be considered in support of the judgment. *Yoder* v. *Nu-Enamel Corp.*, 145 F. 2d 420 (8th Cir. 1944). A cross-appeal was not a condition precedent to this right. *Anderson* v. *Atherton, supra.* The contrary holding of the court below is erroneous.

B. A party litigant does not have an appealable interest unless aggrieved by the judgment of the trial court. *Corning* v. *Troy Iron & Nail Factory*, 56 U.S. 451 (1853); *Public Serv. Com.* v. *Brashear Freight*

Lines, 306 U.S. 204 (1939). Petitioner had a judgment of $27,400 in the district court. Petitioner was aggrieved only by the rulings of the trial court which barred him from recovering the entire amount sought in his *ad damnum,* $36,000. Such rulings may be challenged by appeal or cross-appeals—other rulings may not. The trial court found that money defrauded from Petitioner had been paid to Respondent. Its ruling striking evidence supporting that fact did not affect the *amount* of Petitioner's recovery. Petitioner not being aggrieved, could not appeal this ruling. It was error for the court of appeals to refuse to pass on such evidentiary rulings adverse to Petitioner and to order judgment for Respondent because Petitioner had not filed a cross-appeal.

II

A. The affidavit which was stricken by the trial court is admissible as a declaration against interest.

In the affidavit the Bankrupt who died before trial (R. 35) admitted having obtained $47,980 from Petitioner. He further admitted converting $36,000 of that money to an unauthorized use, *i.e.,* paying it to Respondent. This admission would also deprive the Bankrupt of credit for money paid in under the turnover order. Both statements were against the pecuniary interest of the Bankrupt.

Federal Rule of Civil Procedure 43 declares that where more than one rule of evidence may apply, the one favoring admissibility should govern. Under the law of Illinois, the situs of the district court, as under the law of evidence generally, the affidavit was admissible as a declaration against interest. *Schell* v. *Weaver,* 225 Ill. 159, 80 N.E. 95 (1906); *5 Wigmore on*

Evidence (3rd Ed.) § 1456-1457; 58 Harv. L. Rev. 1, 29-31, 57. The district court erred in striking the affidavit.

B. The affidavit being admissible, the judgment of the district court should be affirmed. The scheme of Federal Rule of Civil Procedure 43(c) is that in actions tried without a jury, evidence ruled inadmissible shall be made part of the record in order that the appellate court may consider the evidence if it is admissible. This practice, early established as a part of Federal equity rules as a method of avoiding circuity in appellate proceedings, has continued under Federal Rule 43(c). *Blease* v. *Garlington*, 92 U.S. 1, 10 (1876); former equity rule 46; Advisory Committee Report accompanying Federal Rule 43(c). Since this affidavit is before this Court, this Court should, upon consideration of the affidavit, affirm the judgment of the district court. *5 Moore's Federal Practice*, p. 1352, *F. H. McGraw* v. *Milcor Steel Co.*, 149 F. 2d 301 (2nd Cir., 1945); cert. den. 326 U.S. 753. If this is done, it is not necessary to consider the following issues relating to the duties of a Trustee in Bankruptcy.

III

Respondent as Trustee in Bankruptcy is an officer of the court. As such he is held to a standard of duty and care commensurate with that office. Respondent had a duty of investigating the source of payments made to him by the Bankrupt under the turnover order.

A. A turnover order is a harsh, coercive remedy. Imprisonment is the penalty of non-compliance. Because of the drastic nature of a turnover order, there is imposed on the Trustee a correlative duty to in-

vestigate the source of money paid in under such an order so that the rights of third parties will not be impinged upon. Cf. *Maggio* v. *Zeitz*, 333 U.S. 56 (1948).

B. The installment payments made to Respondent under the turnover order in this case were made during a period from two to three years after bankruptcy. Respondent had neither title nor right of possession to property acquired by the Bankrupt after bankruptcy. 11 U.S.C.A. § 110. As the date of bankruptcy receded into the past the possibility that money paid in by the Bankrupt was after-acquired property became more of a certainty. In the face of this, Respondent could not act as a mere depository. The office he occupied required that he make the necessary inquiry to ascertain whether money tendered him was properly an asset of the Estate he was administering.

C. Respondent was not only Trustee of the Estate of Robert L. Knetzer, but also was Trustee of the Knetzer Motor Sales Company. Initially these two Estates were separate and distinct, with different creditors and different assets. Since Respondent represented two related estates, it was necessary for him to examine the source of assets tendered to him in order that he could credit the proper estate. Failure to make inquiry would result in unjustly increasing the assets of one estate to the detriment of the other.

D. Respondent had knowledge of facts indicating the Bankrupt was using money of third persons, not concealed assets, to satisfy the turnover order. Respondent knew of Knetzer's activities before bankruptcy. Respondent himself charged that the Bankrupt had concealed $250,000 in estate assets, an ac-

cusation that must have been based on facts affecting the trustworthiness of the Bankrupt. The facts of this case, plus the fact that the Bankrupt and others made small installment payments over a long period of time many months after the entry of the turnover order, gave rise to an inference that money paid in was not estate assets. Respondent thus had the duty of inquiry—a duty Respondent did not fulfill.

IV

Petitioner has adduced sufficient evidence to make out a *prima facie* case that the Bankrupt paid Respondent $27,400 which the Bankrupt had defrauded from Petitioner. Any supposed weakness in Petitioner's case must be weighed against the actions of Respondent. As Respondent failed to make any attempt to ascertain the source of payments made to him, he cannot profit from his failure to do so. Permitting the Bankrupt to pay to him money fraudulently extracted from third parties could only encourage the Bankrupt to commit more fraud.

Bankruptcy proceedings are proceedings in equity. *Local Loan Co.* v. *Hunt*, 292 U.S. 234, 240 (1934). The trial judge who heard the evidence and observed the demeanor of the witnesses held that the equities were with Petitioner. Weighing the evidence Petitioner has adduced against the actions of Respondent, equity and good conscience demand that the judgment of the trial court be affirmed.

Respondent cannot demand other and different proof which is unavailable because he mutely accepted money tendered him instead of making the requisite investigation. The salient fact of the case is that the

transactions occurred subsequent to bankruptcy. The payments being made *after* bankruptcy, Petitioner is relieved of the burden of identifying the funds sought to be recovered. *City of New York* v. *Rassner,* 127 F. 2d 703 (2d Cir. 1942); *United States* v. *Sampsell,* 193 F. 2d 154 (9th Cir. 1951); *Hercules Service Parts Corp.* v. *United States,* 202 F. 2d 938 (6th Cir. 1953). Petitioner has sustained the lesser quantum of proof required by the circumstances. The judgment of the trial court should be affirmed.

ARGUMENT

THE COURT OF APPEALS ERRONEOUSLY REFUSED TO CONSIDER APPELLEE'S CONTENTIONS IN SUPPORT OF THE VERDICT OF THE TRIAL COURT BECAUSE PETITIONER FILED NO CROSS-APPEAL

Petitioner was victorious in the trial court, obtaining a judgment of $27,400. The findings of fact supporting the judgment were favorable to Petitioner. The trial judge, however, after tentatively receiving in evidence an admission by the deceased Bankrupt, Knetzer, that he had paid $36,000 of Petitioner's money to Respondent, ordered the evidence stricken.

Respondent appealed from the adverse judgment. The appellate court ruled that the evidence did not support the finding that the Bankrupt had turned over $27,400 of Petitioner's money to Respondent Trustee, erroneously refusing to pass on the propriety of the trial court's ruling striking the Bankrupt's admission, evidence highly pertinent to the issue. The stated basis for the court's refusal to consider this ruling was Petitioner's failure to cross-appeal from the trial court's ruling striking the evidence.

A. Petitioner Could Urge Any Matter Before the Trial Court In Support of His Verdict

Having obtained a verdict in the district court, Petitioner was, without a cross-appeal, at liberty to support that verdict before the appellate court on any ground raised before the trial court. *United States* v. *American Ry. Exp. Co.*, 265 U.S. 425 (1924); *Anderson* v. *Atherton*, 302 U.S. 643 (1937); *Mount Pleasant* v. *Beckwith*, 100 U.S. 514 (1880); *Helvering* v. *Pfeiffer*, 302 U.S. 247 (1937). Petitioner had standing to attack the reasoning of the lower court and support the judgment by adverting to matters overlooked or ignored by the trial court. *United States* v. *American Ry. Exp. Co., supra.* This rule is "inveterate and certain". *Morley Constr. Co.* v. *Maryland C. Co.*, 300 U.S. 185 (1937).

Petitioner could not, of course, be heard in opposition to the judgment nor attempt to enlarge his, or diminish Respondent's rights under the judgment. *United States* v. *American Ry. Exp. Co., supra; Langnes* v. *Green*, 282 U.S. 531 (1931).

But Petitioner did not attack the judgment of the trial court in the appellate court. To the contrary, he sought to support the judgment by contending that certain evidence stricken by the trial court was admissible. Petitioner did not seek a revision of the findings of the trial court which "carries with it as an incident a revision of the judgment". *Morley Constr. Co.* v. *Maryland C. Co., supra*, 300 U.S. at 192; cf. *Partmar Corp.* v. *Paramount Theatres Corp.*, 347 U.S. 89, 99 (1954). The findings were favorable to Petitioner. He merely sought to have evidence supporting those findings declared admissible. The affidavit

was designated for inclusion in the record on appeal (R. 176).

Petitioner did not before the court below and does not here attack either the judgment or the findings of the trial court. Petitioner merely asserts an additional ground, ignored by the trial court, why the decree should be affirmed. *Anderson* v. *Atherton, supra; United States* v. *Carignan,* 342 U.S. 36 (1951).

It has been specifically held that in absence of a cross-appeal courts of review will, at the instance of appellees, pass on evidentiary rulings of the trial court. *Yoder* v. *Nu-Enamel Corp.,* 145 F. 2d 420 (8th Cir. 1944). See *Lanova Corp.* v. *National Supply Co.,* 116 F. 2d 235 (3rd Cir. 1940); *Cusack* v. *Longaker,* 95 F. 2d 304 (2nd Cir. 1938). Since Petitioner had the right to urge that all evidence supporting the findings be considered, including that improperly stricken, the court of appeals fell into error in refusing to consider that issue.*

It was the correctness of the judgment which Respondent's appeal challenged, not the basis upon which it rested. *In re Schwartz,* 89 F. 2d 172 (2nd Cir. 1937); *Century Distilling Co.* v. *Continental Distilling Co.,* 106 F. 2d 486 (3rd Cir. 1939); *cert.* den. 309 U.S. 662 (1940). Petitioner had the right to support the judgment by urging consideration of erroneous evidentiary rulings of the trial court, if any. A cross-appeal was not a condition precedent to that right. The contrary ruling of the appellant court must be reversed.

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* The Court of Appeals must affirm the judgment if it finds in the record any reason which it considers sound, even though the district judge may have rejected that reason and rested his decision on some other ground. *Dean* v. *Davis,* 212 Fed. 88, 89 (4th Cir. 1914); aff. 242 U.S. 438 (1917).

B. Petitioner, Not Being An Aggrieved Party, Had No Standing To Cross-Appeal From the Judgment of the District Court

Petitioner was the prevailing party in the district court. The judgment as well as the findings of the district court were favorable to Petitioner.

A successful party in the trial court has no standing to appeal from a decree in his favor.* In order to have standing to appeal, a party must be aggrieved by the judgment entered. *Corning* v. *Troy Iron & Nail Factory,* 56 U.S. 451, 14 L. Ed. 768 (1853); *Zoline's Fed. App. Juris. & Proc.* (3rd Ed.) § 138, or by findings of fact necessary to the decree. *Partmar Corp.* v. *Paramount Theatres Corp.,* 347 U.S. 89 (1954), but cf. dissenting opinion 347 U.S. at 109; *Morley Constr. Co.* v. *Maryland C. Co., supra.* Petitioner, aggrieved by neither, could not cross-appeal.

To be sure, Petitioner could have appealed from the failure of the district court to award him the entire sum demanded in his complaint. But the action of the trial court refusing recovery of the entire sum and

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* *Public Service Com.* v. *Brashear Freight Lines,* 306 U.S. 204 (1939); *New York Teleph. Co.* v. *Maltbie,* 291 U.S. 645 (1934); *Lindheimer* v. *Illinois Bell Teleph. Co.,* 292 U.S. 151 (1934); *Harding* v. *Federal National Bank,* 31 F. 2d 914 (1st Cir. 1929); *In re Schwartz,* 89 F. 2d 172 (2nd Cir. 1937); *Lanova Corp.* v. *National Supply Co.,* 116 F. 2d 235 (3rd Cir. 1940); *United Engineering and Foundry Co.* v. *Cold Metal Process Co.,* 68 F. 2d 564 (3rd Cir. 1934), *cert.* den. 291 U.S. 675; *Aberly* v. *Craven County,* 70 F. 2d 52 (4th Cir. 1934); *Ottenheimer Bros.* v. *Libuwitz,* 74 F. 2d 858 (4th Cir. 1935), *cert.* den. 296 U.S. 582; *Mach* v. *Abbott Co.,* 136 F. 2d 7 (8th Cir. 1943), *cert.* den. 320 U.S. 773; *United States* v. *Adamant Co.,* 197 F. 2d 1 (9th Cir. 1952), *cert.* den. 344 U.S. 903 (1952).

rendering a judgment for $27,400 was correct.* The evidence supports the court's ruling on this issue and Petitioner was and is content with the judgment. It is established that parties who are satisfied with their judgment cannot confer jurisdiction on appellate courts to decide alleged errors in the trial by cross-appealing their favorable judgment. *Midland Valley R. Co.* v. *Fulgham,* 181 Fed. 91 (8th Cir. 1910).

Even more basic, however, is that Petitioner had nothing to appeal from. Any cross-appeal would be limited to demonstrating error in the court's failure to grant a judgment for $36,000. The evidentiary ruling striking the Bankrupt's affidavit from evidence had no bearing on the amount of recovery. Other evidence indicated to Petitioner that the trial court's finding in this regard was correct. Consequently, the ruling on the affidavit would not even be relevant to the issues raised by Petitioner's cross-appeal.

Since Petitioner, not being aggrieved, had no standing to cross-appeal, the holding of the appellate court that Petitioner should have cross-appealed at penalty of waiver is erroneous. This error was compounded by the revising of the mandate at Respondent's request so as to peremptorily order that judgment be entered for Respondent instead of remanding the cause for further proceedings as the original opinion had directed.

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* A mathematical deduction indicates that the trial court refused recovery of the December 7, 1950 payment of $3,800 which was to be paid into court, and the payment of $4,800 on October 1, 1951 which was secured by a mortgage which Petitioner later surrendered (R. 54, 109, 127, 132).

By effectively barring appellate review of the erroneous evidentiary ruling of the trial court, the court of appeals has deprived Petitioner of his day in court.

II. THE JUDGMENT OF THE DISTRICT COURT SHOULD BE AFFIRMED

A. The Declaration Against Interest of the Bankrupt Was Admissible Against His Trustee

Federal Rule of Civil Procedure 43(a) states that evidence in district courts shall be admitted where admissible under statutes of the United States, former rules of evidence in equity or under rules of evidence of the courts of the jurisdiction in which the district court is held. The statute or rule *"which favors the reception of the evidence governs"*.* The affidavit of the Bankrupt, Petitioner's Exhibit 24, stricken below, is clearly admissible under Illinois law.

The affidavit of the bankrupt, an extrajudicial statement under oath, is admissible as a declaration against interest. Even an *unsworn* oral statement would be admissible under this well-defined exception to the hearsay rule. The statement is clearly a declaration against interest. The Bankrupt admitted obtaining over $47,980 from Petitioner and a breach of his obligation to Petitioner to utilize the funds for the fictitious Bison Development Corporation.**

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* Emphasis added.

** The affidavit in question executed by the Bankrupt under oath on August 1, 1952, is as follows:

> "That during the period from December 7, 1950, to October 23, 1951, I, Robert L. Knetzer, borrowed the sum of $47,980.00 (Forty-seven thousand nine hundred eighty & no/100 dollars) from Robert W. Jaffke, of St. Louis, Missouri, and that during the period of December 7, 1950 to November 1, 1951, I paid

In the affidavit the Bankrupt admitted that he had obtained $47,980.00 from Petitioner. It appearing that the Bankrupt-declarant was dead at the time of trial (R. 35), it is settled Illinois law that an admission by the decedent that he had obtained money from Petitioner is admissible as a declaration against interest. *Schell* v. *Weaver*, 225 Ill. 159, 80 N.E. 95 (1906). The rule is overwhelmingly accepted in other jurisdictions. 5 *Wigmore on Evidence* (3rd Ed.) Sec. 1456-1457.*

As one portion of the affidavit was admissible as a declaration against interest the entire declaration was admissible. As Wigmore puts it:

> "In other words, the statement may be accepted, not merely as to the specific fact against interest, but also *as to every fact contained in the same statement.*" 5 *Wigmore on Evidence* (3rd Ed.) Sec. 1465.**

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the sum of $36,000.00 (Thirty-six thousand dollars) from the above borrowed sum of $47,980.00 to Wm. C. Dunham, Trustee in Bankruptcy of Robert L. Knetzer, for purposes of remaining out of jail. I am of sound mind and body and no threats or promises were made to me in order to obtain this statement."

* "The clearest case of a declaration stating a liability of the declarant is one conceding a liquidated indebtedness of the declarant to another. 'I owe John Smith $100' is a typical declaration against pecuniary interest. Declarations of general indebtedness, such as 'I am indebted to John Smith', are equally admissible. A declaration need not concede specifically an indebtedness in order to come within the concept of pecuniary interest. A statement of facts which clearly create a contractual liability of the declarant is considered equally contrary to pecuniary interest." 58 Harv. Law. Rev. 1, at pages 29-30.

** "From the very beginning of this exception, it has been held that a declaration against interest is admissible, not only to prove the disserving fact stated, but also to prove other facts contained in collateral statements connected with the disserving statement." 58 Harv. Law. Rev. at 57.

The statement in the affidavit that the Bankrupt "paid the sum of $36,000 (thirty-six thousand dollars) from the above borrowed sum of $47,980.00 to Wm. C. Dunham, Trustee in Bankruptcy of Robert L. Knetzer . . ." is equally admissible as a declaration against interest. Petitioner's testimony which was accepted by the trial and appellate courts was that the money defrauded from him by the Bankrupt was to be used in the furtherance of the objectives of the Bison Development Company. That the declaration was against the declarant's interest may of course be shown by independent evidence. 5 *Wigmore on Evidence* (3rd Ed.) § 1468. By the affidavit the Bankrupt admitted that he had improperly diverted a portion of the funds obtained from Petitioner to the Respondent. That declaration would thus subject the Bankrupt to an action for fraud and is consequently admissible as a declaration against his interest even apart from the related declaration that he had obtained $47,980 from Petitioner. *Citizens National Bank* v. *Santa Rita Hotel Co.*, 22 F. 2d 524 (9th Cir. 1927).* Even more convinc-

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* "On principle, it would seem that a declaration conceding a tortious liability stands on the same footing as a declaration conceding a contractual obligation. The pecuniary interest of the declarant is affected in the same manner by both types of declarations. The likelihood of the declarant's having to respond for his tortious conduct is equally as strong as for his liability in contract. This is certainly true if the declaration relates a clear and obvious case of tortious liability. The courts have had no difficulty in classifying declarations stating facts creating a tortious liability in a definite amount within the concept of pecuniary interest. A number of decisions have held admissible declarations by employees that they had embezzled or stolen stated amounts of money from their employers. Even in the case of declarations relating to tortious liability in an unliquidated amount, the courts have usually admitted such declarations where intentional torts were conceded by the declarations." 58 Harv. Law Rev. 1 at page 31.

ing is that the declaration would have *deprived the Bankrupt of a credit of $36,000 under the turnover order* thus subjecting him to longer imprisonment. The affidavit being clearly admissible as a declaration against interest, the trial court erred in striking such affidavit from the record.

The circumstances surrounding the execution of the affidavit also attest to its trustworthiness. R. W. Heinze, an Illinois attorney, was handed the unsigned affidavit by Petitioner who had prepared it on the basis of information supplied him by the Bankrupt. (R. 112). Heinze was on his way to confer with the Bankrupt, who on this particular time was again in jail. Heinze showed Knetzer the affidavit and, in response to an inquiry by Knetzer as to whether he should sign it, Heinze told him "you cannot sign anything unless it is true". (R. 103-104). Heinze obtained permission from "officials of the government" to present the affidavit to Knetzer. (R. 104). Mr. Heinze was present when the Bankrupt was sworn to the truth of the facts stated in the affidavit by the notary public (R. 104). Heinze then returned the signed and notarized affidavit to Petitioner (R. 105). The notary public testified that he had sworn the Bankrupt to the truth of the contents of the affidavit and then notarized it (R. 74-75).

The affidavit was clearly admissible.

B. Since the Evidence Was Properly Admissible the Judgment of the District Court Should Be Affirmed

Since, as has been demonstrated, the affidavit of the Bankrupt Knetzer admitting that he had turned $36,000 of Petitioner's money over to the Trustee in

Bankruptcy was improperly stricken, the next question is the proper disposition of the case. As appears from the record the affidavit was admitted into evidence and was not stricken until after trial had concluded. Petitioner designated the affidavit to be included in the appellate record (R. 176). Respondent, while the affidavit was in evidence, had the opportunity to contradict it or adduce evidence going to the weight to be accorded the affidavit. He did neither. Since there is no evidence in the record (nor elsewhere) to contradict the admission that Petitioner's money was turned over to Respondent the only proper disposition of the case is to affirm the judgment of the district court.*

Where evidence which has been excluded or stricken by the trial court is before the appellate court, the reviewing court should consider such evidence and, if possible, make a decision as though such evidence had been properly admitted in the first instance. It was early established by this court that the appellate tribunal, if necessary, should consider excluded evidence and render a decision based thereon to avoid the circuity of action which would otherwise result. *Blease* v. *Garlington*, 92 U.S. 1, 10 (1876). Nothing but delay and added expenses would ensue if this case were remanded to either the appellate court or to the district court to reopen the record, to consider the uncontroverted evidence contained in the affidavit, and to render judgment accordingly.

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* At the trial Respondent refused to deny that he had testified at an earlier proceeding that the Bankrupt had given him money which the Bankrupt stated had been obtained from Petitioner (R. 88-89).

In *Blease* v. *Garlington, supra,* this Court adverted to the fact that it had earlier adopted equity rules requiring a record to be made of excluded evidence which would be transmitted to the reviewing court if an appeal were taken. The purpose was to allow appellate tribunals to pass on the excluded evidence if necessary to reach a decision, thus avoiding remanding the case for further hearing. See also *Nelson* v. *United States,* 201 U.S. 92, 114, 115 (1906). The practice approved in *Blease* v. *Garlington, supra,* continued as an integral part of federal equity practice. See Supreme Court Equity Rule 46, 28 U.S.C. Section 730 (1934 ed.). With the adoption of the Federal Rules of Civil Procedure in 1938, the practice has been continued until the present time. Thus Federal Rule of Civil Procedure 43(c) provides:

> "Record of Excluded Evidence. In an action tried by a jury, if an objection to a question propounded to a witness is sustained by the court, the examining attorney may make a specific offer of what he expects to prove by the answer of the witness. The court may require the offer to be made out of the hearing of the jury. The court may add such other or further statement as clearly shows the character of the evidence, the form in which it was offered, the objection made, and the ruling thereon. In actions tried without a jury the same procedure may be followed, except that the court upon request shall take and report the evidence in full, unless it clearly appears that the evidence is not admissible on any ground or that the witness is privileged."

That the above rule was designed to continue the practice under former Equity Rule 46 is clear from the report of the Advisory Committee accompanying Rule

43(c).* The requirement of the Rule is that the lower court should, at minimum, make a record of all evidence proffered in order that appellate court if it disagrees with the lower court's conclusion may render a proper judgment without remanding the case for further trial. 5 *Moore's Federal Practice,* 2nd Ed., p. 1352. If the excluded evidence is, as here, before the appellate court, the court should consider it if admissible, even where it has been excluded by the trial court. *ibid.; F. H. McGraw* v. *Milcor Steel Co.,* 149 F. 2d 301 (2d Cir. 1945); cert. den. 326 U.S. 753. See also *Kauk* v. *Anderson,* 137 F. 2d 331, 334-335 (8th Cir. 1943); *Thompson* v. *Carley,* 140 F. 2d 656 (8th Cir. 1944); *Garden City Feeder Co.* v. *Commissioner of Internal Revenue,* 75 F. 2d 804, 807 (8th Cir. 1935); *United States* v. *Jones,* 176 F. 2d 278 (9th Cir. 1949); *First National Bank of Atlanta* v. *Southern Cotton Oil Co.,* 78 F. 2d 339 (5th Cir. 1935); *Hughes* v. *Reed,* 46 F. 2d 435, 442 (10th Cir. 1931).

As the court stated in *Unkle* v. *Wills,* 281 Fed. 29 (8th Cir. 1922), cited by the Advisory Committee in its note to Federal Rule 43(c):

> "It is equally well settled that, even if objections to evidence are sustained in equity cases, it is the duty of the court to have them answered and included in the record, so that, if the appellate court

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* The Advisory Committee report states: "Note to Subdivision (c). See Equity Rule 46 (Trial-Testimony Usually Taken in Open Court-Rulings on Objections to Evidence). With the last sentence compare Dowagiac v. Lochren, 143 Fed. 211 (CCA 8th, 1906). See also Blease v. Garlington, 92 U.S. 1 (1876); Nelson v. United States, 201 U.S. 92, 114 (1906); Unkle v. Wills, 281 Fed. 29 (CCA 8th, 1922)."

finds that the chancellor erred in his rulings, the cause need not be remanded to have the requested testimony retaken." (p. 34).

Since the rule under the former equity practice permitting the appellate court to consider excluded evidence in reaching its decision has been embodied in current practice by Federal Rule of Civil Procedure 43(c), it follows that this court should, after considering the declaration against interest of the Bankrupt Knetzer, affirm the judgment of the district court.

III. A TRUSTEE IN BANKRUPTCY HAS THE DUTY OF INVESTIGATING THE SOURCE OF PAYMENTS MADE TO HIM IN PURPORTED COMPLIANCE WITH A TURNOVER ORDER

A Trustee in Bankruptcy has a responsibility to prevent his office from being used in derogation of the rights of third parties. Respondent generally, and particularly under the facts of this case, had the duty of investigating the source of assets tendered to him in his official capacity.

A. The Compulsion of a Turnover Order Imposes a Correlative Duty on the Trustee in Bankruptcy To Investigate the Source of Funds Paid Under the Order

After Knetzer was adjudged bankrupt on October 21, 1948 (R. 165), a turnover order was entered July 11, 1949, directing the Bankrupt to pay $250,000 to Respondent as Trustee in Bankruptcy, "forthwith" (R. 144). Respondent filed a motion to show cause and the Bankrupt was held in contempt of court on December 1, 1949, for failing to comply with the turnover order (R. 145-148). His imprisonment was stayed until March, 1950, at which time the Bankrupt was imprisoned. (R. 165). He was released from jail for varying periods of time in order to obtain money

to buy his freedom by making installment payments to the Trustee.

A turnover order addressed to a bankrupt is as drastic a coercive remedy as the bankruptcy court may invoke. In turnover proceedings "coercive methods by imprisonment are probable and are foreshadowed." *Oriel* v. *Russell,* 278 U.S. 358, 363 (1929). Common knowledge reveals that a threat of incarceration may drive one beyond the pale of the law in a distraught effort to avoid loss of freedom.

A trustee in bankruptcy is an officer of court. As such he has a special duty imposed upon him in cases where a turnover order has been entered. That duty is the protection of innocent third parties and perhaps the bankrupt whose actions to avoid imprisonment may lack the rational, well-considered judgment of an individual not acting under judicial duress.

This Court in *Maggio* v. *Zeitz,* 333 U.S. 56 (1948) recognized the possibility that a turnover order—with its implied threat of imprisonment for non-compliance —could "exert pressure on friends and relatives to ransom the accused party from being jailed". 333 U.S. at 64. In the absence of friends and relatives the bankrupt who is unable to comply with the order must fall back on his own resources. One result is found in the facts of this case. Petitioner, an innocent third party, was defrauded by the Bankrupt during the period December 7, 1950 to November 1, 1951. The fraud was accomplished when the Bankrupt, a civil contemnor, had been released from prison for the express purpose of obtaining funds to satisfy the turnover order. Respondent even used his own office to obtain extensions of time during which the Bankrupt

could remain out of prison. Had the Bankrupt a penchant for the use of violence rather than fraud, a more tragic situation could be spread on this record.

It is of course impossible to insure absolutely that the bankrupt will not perform criminal or "shady" acts in his frantic efforts to satisfy a turnover order and avoid jail. A strong deterrent, however, would be a searching inquiry by the trustee into the source of moneys paid into him in purported compliance with a turnover order. Knowledge by the bankrupt that monies obtained by fraud or other criminal conduct would be unacceptable to the trustee would stifle any incipient tendency to criminality.

It is abhorrent to established concepts of justice and fairness that a trustee in bankruptcy may act as a mere conduit of money or property—becoming thus, albeit unwittingly, a depository for the property of an innocent third party.* The office of trustee in bankruptcy is not so circumscribed as to prohibit investigation and an exercise of discretion as to what funds are properly assets of the estate being administered. The contrary is obviously true.

The trustee may not stand mute and accept property paid to him under judicial duress, assuming it properly comes into his custody. The discretion of the office must be exercised, by testing, by probing to ascertain the source and ownership of property paid into him under duress, *i.e.*, under the compulsion of a turnover order. That the rights of innocent third

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* "Let the hand receiving it be ever so chaste, yet if it comes through a corrupt polluted channel, the obligation of restitution will follow it." *Bridgman* v. *Green*, 2 Ves. Sr. 627, Wilm. 58, 65 (1755).

parties will not be impaired, that the creditors of the estate will not be unjustly enriched, the trustee must comply with the duty of scrutiny which is imposed upon him by virtue of his office.

B. The Trustee Had the Duty of Ascertaining If Monies Paid to Him Constituted After Acquired Property

While the element of duress in compliance with turnover orders imposes a correlative duty of inquiry on the Trustee, the facts of this case disclose additional bases upon which such a duty rests.

Knetzer was adjudged a bankrupt October 21, 1948. On July 11, 1949, the turnover order in question was entered. Approximately seventeen months after the turnover order, during the period commencing December 7, 1950, the Bankrupt was still making the installment payments to Respondent which are the subject of this controversy. These payments continued to October 23, 1951. Indeed, other payments were made until February, 1952.

Respondent had no title to any property acquired by the Bankrupt after his adjudication as such, with certain exceptions not here applicable. 11 U.S.C.A., § 110; 4 *Collier on Bankruptcy* (14th ed.), § 70.09; *Clay* v. *Waters,* 161 Fed. 815 (8th Cir. 1908). As to property coming into his possession, Respondent was not considered an innocent purchaser for value. *Zartman* v. *First Nat. Bank,* 216 U.S. 134 (1910). Since Respondent had no authority to accept after acquired property of the Bankrupt, having neither title thereto nor right of custody thereof, he had the obvious duty of ascertaining whether property tendered to him was after acquired property or not. This duty of inquiry becomes more pronounced and

more important as the date of the bankruptcy recedes into the past. For as time passes the possibility that property possessed by the Bankrupt was acquired subsequent to his bankruptcy becomes more certain. With the passage of sufficient time this possibility ripens into a certitude.

Respondent could not ignore this fact in accepting money paid to him as Trustee *from two to three years after* the Bankrupt had been adjudged as such. Certainly the possibility that the money paid Respondent in 1950 and 1951 by the Bankrupt was acquired subsequent to his bankruptcy had become strong enough to require an initial scrutiny by Respondent to ascertain if the money was properly his. The duty to locate and marshal assets, *Avery* v. *Cleary*, 132 U.S. 604 (1890), of necessity carries with it the duty to ascertain whether the Trustee has the right to possess the property.

The entry of the turnover order on July 11, 1949, did not affect this duty. The Bankrupt was adjudged in contempt for failure to comply with the order in December, 1949. The Bankrupt was imprisoned in March of 1950 but was released at varying times supposedly to locate the hidden assets required to be paid to Respondent under the turnover order. Whatever presumption there might be that the Bankrupt had $250,000 in July of 1949, it could not continue *ad infinitum* to relieve Respondent of his duty to inquire into the source of funds paid to him. Imprisonment of the Bankrupt and passage of sufficient time would certainly dispel any such presumption. Cf. *Maggio* v. *Zeitz, supra.*

Respondent, after the Bankrupt was jailed as a contemnor and after seventeen months had elapsed since

the entry of the turnover order, could not blindly accept money tendered him without ascertaining whether such money was properly his. Respondent had no right to take property not belonging to the Bankrupt. *In re Allee,* 55 F. 2d 76 (7th Cir. 1932). His was the duty of inquiry, a duty singularly unfulfilled.

C. Respondent, as Trustee of Two Related Estates, Was Required To Ascertain To Which Estate Assets Tendered Him Should Be Credited

Yet another basis for Respondent's duty of inquiry is presented on the record. Respondent was appointed Trustee of Knetzer Motor Sales Company on December 3, 1948, and Trustee of the Estate of Robert L. Knetzer on December 10, 1948 (R. 76).

The turnover order of July 11, 1949, required the Bankrupt to pay the $250,000 to Respondent *as Trustee of the Estate of Robert L. Knetzer.* The order expressly declared that Respondent *as Trustee for Knetzer Motor Sales Company was "not entitled to* any turnover order against Robert L. Knetzer" (Pet. Exh. 1, R. 144, 135-6).

It should be emphasized that the assets of the two Estates, that of Robert L. Knetzer and that of the Knetzer Motor Sales Company, initially, were considered to be separate and distinct. Creditors of the two Estates were not identical. (R. 138, 161-164; Defs. Exh. 1). Because of the dual role of the Trustee—representing two Estates and two different groups of creditors the Trustee had the obvious duty of inquiry to ascertain which assets coming into his hands belonged in which Estate. Assets tendered to the Trustee were required to be identified and credited to the proper Estate. Failure to properly differentiate be-

tween the assets of the two Estates would result in an unjust benefit to one Estate in derogation of the rights of creditors of the other.

This dual representation placed an initial duty on the Respondent of inquiry into the source of assets coming into his custody. A proper identification of the source of the assets was a necessity if Respondent were properly to segregate the assets of the Estates under his control. Even a token compliance with this duty is lacking here.

D. The Trustee Had Knowledge of Facts Putting Him on Notice that the Bankrupt Was Not Paying in Concealed Assets

Respondent had knowledge of sufficient facts to put him on knowledge, actual or constructive, that the Bankrupt was not paying in concealed assets. Respondent certainly had knowledge of Knetzer's fraudulent activities before bankruptcy (R. 182). Respondent knew that a large number of claims against the two Estates had been filed and that the assets of those Estates were but a small fraction of such claims (Def. Exh. 1, R. 161-164). The proceedings culminating in a turnover order were initiated by a petition verified by Respondent. Consequently, he must have had, at minimum, reason to believe that the Bankrupt had concealed assets and was a person not to be trusted (Pet. Exh. 1, R. 144, 317).

As early as April, 1950 Respondent heard testimony of third parties and the Bankrupt under oath that the latter had been "borrowing" from such third parties (R. 38-39, 84, 90-91). If verification of this testimony were needed, it came when third persons made payments to Respondent under the turnover

order (R. 80, 82-84). In one instance, a third party making such payments (Rhoades) told Respondent that he was making payments for the Bankrupt and that "he would be responsible for a thousand dollars a day" (R. 84).

The Bankrupt informed Respondent that he was engaged in many "business ventures", including the "Christmas tree" and "Teapot Dome" "deals" (R. 83, 86). While Respondent knew that the Bankrupt had been imprisoned for failure to comply with the turnover order, he knew that the Bankrupt was "in and out of jail" and while out of jail was not in the custody of a marshal (R. 77, 85).

Perhaps the most significant fact, however, is that Respondent refused to deny that he may have testified before a grand jury in 1952 that he had received in excess of $5,000 from the Bankrupt in 1951, which the Bankrupt told him had been obtained from Petitioner (R. 88-89).

At minimum, Respondent had knowledge from the above facts that the Bankrupt was not to be trusted. Cf. *Watchmaker* v. *Barnes,* 259 Fed. 783 (1st Cir. 1919). *1 Merrill on Notice,* § 173. The facts were sufficient to excite inquiry in a prudent man. A concomitant duty to investigate immediately arose. Cf. *Avery* v. *Cleary,* 132 U.S. 604 (1890).*

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* Respondent, of course, had the statutory duty of reporting possible violations of the bankruptcy laws of the United States to the appropriate United States Attorney. 18 U.S.C.A., § 3057.

IV. RESPONDENT MAY NOT PROFIT FROM HIS FAILURE TO MAKE THE NECESSARY INQUIRY DEMANDED BY THE CIRCUMSTANCES OF THIS CASE

It is undisputed that Respondent failed to make even the most rudimentary investigation of the source of funds paid to him under the turnover order. He admitted at the trial that he had made no such inquiry when payments were made to him (R. 87, 79-80). He also admitted that he never had any evidence that the payments made to him under the turnover order constituted concealed assets of the Estate (R. 93-94). Respondent knew that when the Bankrupt was out of jail he was not in the custody of a United States Marshal (R. 77, 85). There is no evidence that Respondent reported this fact to any responsible authorities. The opposite is true, for Respondent admitted that he called his attorney or the district judge on several occasions to obtain permission for the Bankrupt to remain out of jail (R. 85). Respondent, in the face of a duty to inquire into the source of payments made to him, and ignoring completely facts which would have excited the interest of a prudent man, as an officer of the court cannot now in equity and good conscience be permitted to retain funds which he should have known were not properly part of the Estate in bankruptcy. To deny Petitioner recovery in this case, would be "condoning improper action by a trustee so long as he could successfully get away with it." *City of New York* v. *Rassner,* 127 F. 2d 703 (2nd Cir., 1942).

It appears that the evidence in this case *at a minimum* establishes *prima facie* that Respondent holds Petitioner's money. Before his death, the Bankrupt admitted paying over Petitioner's money to Respond-

ent. No one was in a better position than the Bankrupt to testify to this fact.

The record of payments to the Trustee is also strong evidence that Petitioner's money had been paid in under the turnover order. Thus, between May 28, 1950, and September 15, 1950, Riley paid Knetzer $32,389. Knetzer paid to the Trustee under the turnover order $32,076.28 between July 28, 1950, and October 28, 1950 (R. 193). It is no mere coincidence that the two figures are so nearly identical.

Petitioner paid the Bankrupt $47,980 between December 7, 1950 and October 22, 1951. During that same period from April 14, 1951 to June 1951, Petty paid the Bankrupt $44,000. Respondent testified that in the period corresponding to the time Petitioner was making payments to Knetzer, December 7, 1950 through October, 1951, he had received a total of $75,923.72 under the turnover order (R. 87). Subtracting the $44,000 which Petty paid the Bankrupt from the total received by Respondent during the period in question, that is $75,923.72, there is a balance of $31,923.72. Certainly these facts considered with other evidence adduced by Petitioner corroborate strongly the fact that the Bankrupt paid a substantial part of Petitioner's money to Respondent.*

It was stipulated at the trial that one Sammons would testify that he had paid the Bankrupt $101,550 between *November* 1, and February 1, 1952 (R. 138). Any payments made from Sammons' money would be

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* All these payments were a record in the bankruptcy proceedings, and the trial court could take judicial notice of them. Freeman-Sweet Co. v. Luminous Unit Co., 264 Fed. 107 (7th Cir. 1919); cert. den. 253 U.S. 486.

beyond the period involved in this suit. Also beyond the period involved in this suit were the payments by Rex Rhoades, whose first payment to Respondent was made on November 13, 1951 (R. 82). When the payment record is thus analyzed it supports the declaration by the Bankrupt that he turned $36,000 of Petitioner's money over to the Trustee. The court of appeals analysis is thus incorrect.

Respondent cannot defend by helplessly declaring that he does not know to whom money paid in under the turnover order belongs when he had the duty of ascertaining that very fact.* Any weakness in Petitioner's proof must be weighed against the fact that Respondent may not profit from his own dereliction. This is inherent in the case since bankruptcy proceedings are governed by equitable principles. *Pepper* v. *Litton,* 308 U.S. 295 (1939); *Local Loan Co.* v. *Hunt,* 292 U.S. 234, 240.**

In weighing the evidence another factor cannot be ignored. The salient, undisputed fact is that the fraud and the installment payments to Respondent occurred *after,* not before, bankruptcy. Such acts occurred while the Bankrupt, an adjudged contemnor, was either in jail or in the actual or constructive custody of the bankruptcy court. In these circumstances, Peti-

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*In Petitioner's Exhibit 29 (R. 204, 167) also stricken by the trial court, Mr. Doyle, United States Attorney, pointed out to the court in an earlier proceeding that the Bankrupt had promised in June, 1950, to pay in $225,000 within six days (R. 206).

**Significantly, the trial judge who heard the evidence and observed the demeanor of the witnesses specifically held that the equities of the case were with Petitioner (R. 166).

tioner, as the beneficiary of a constructive trust, need not identify his money in the hands of Respondent. *City of New York* v. *Rassner,* 127 F. 2d 703 (2d Cir. 1942); *United States* v. *Sampsell,* 193 F. 2d 154 (9th Cir. 1951); *Hercules Service Parts Corp.* v. *United States,* 202 F. 2d 938 (6th Cir. 1953). The determining fact in each of the last cited cases was that the trust relationship arose *subsequent* to bankruptcy. In the *Hercules* case, there was no evidence that the "assets of the debtor were augmented by the payments." 202 F. 2d at 940. The court there emphasized that if the beneficiaries' claim were upheld, the creditors would "receive no less than that to which they were originally entitled and that which they would have received if the officer of the law had performed his obligation." 202 F. 2d at 941.*

Under the doctrine of the last-cited cases the quantum of proof necessary for Petitioner to sustain his case is substantially less than if the fraud had occurred *prior* to bankruptcy. See *Standard Oil Co.* v. *Hawkins,* 74 Fed 395 (7th Cir. 1896).

Weighing Petitioner's evidence against the conduct of Respondent acting as an officer of the bankruptcy court, as must be done in a proceeding "inherently" one in equity, *Local Loan Co.* v. *Hunt, supra,* it is clear that the judgment of the trial court was correct. To permit Respondent, an officer of the court, to retain property accepted with neither inquiry nor investigation when the circumstances commanded both would be a vicious and inequitable result.

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* Significantly, District Judge Briggle stated in an earlier proceeding, money "unlawfully obtained" is "not acceptable to the trustee . . ." (R. 206).

As the court stated in *Ex Parte James,* 9 Ch. App. 609, quoted in *Standard Oil Co.* v. *Hawkins, supra*:

> "That a trustee in bankruptcy is an officer of the court. He has inquisitorial powers given him by the court, and the court regards him as its officer, and he is to hold money in his hands upon trust for its equitable distribution among creditors. The court, then, finding that he has money in his hands which, in equity, belongs to some one else, ought to set an example to the world, by paying it to the person really entitled to it. In my opinion, a court of bankruptcy ought to be as honest as other people."

The judgment of the trial court should be affirmed.

CONCLUSION

The court of appeals' refusal to consider evidentiary rulings in the absence of a cross-appeal is patently erroneous. Since the disputed evidence is before this Court and is clearly admissible, the judgment of the district court should be affirmed. An additional ground for affirming the judgment of the district court is the failure of the Respondent as Trustee to shoulder the duty of inquiry that was his. The judgment of the trial court was correct.

Respectfully submitted,

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